Supreme Court, U.S.
FILED
APR 29 1986
JOSEPH F. SPANIOL, JR.
CLERK

No. 85-1443 (2)

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1985

CORDIS CORPORATION,
Petitioner,
vs.
MEDTRONIC, INC.,
Respondent.

BRIEF OF RESPONDENT IN OPPOSITION

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RESTATEMENT OF QUESTIONS PRESENTED

1. Did the Federal Circuit's decision to vacate the District Court's Order (i) granting interlocutory relief permitting Petitioner to deposit into escrow future royalty payments due Respondent under the License Agreement between the parties, and (ii) enjoining Respondent from terminating the License Agreement, produce a result in conflict with this Court's decision in Lear, Inc. v. Adkins?
2. Was the Federal Circuit's decision to reverse the District Court's grant of relief pendente lite on grounds that the District Court had misjudged the evidence and committed errors of law in its application of the traditional standard for injunctive relief erroneous?

PARTIES TO THE PROCEEDING

See Petition at page ii.[1]

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1. Pursuant to Supreme Court Rule 28.1, Medtronic, Inc. has no parent company or subsidiaries, except wholly owned subsidiaries. It holds small minority interests in Bio-Medicus, Inc., located in Minnetonka, Minnesota; Bio-Nexus located in Raleigh, North Carolina; Xenotech, located in Irvine, California; Life Science Instrumentation, Inc., located in Portland, Oregon; and City Venture Corporation, located in Minneapolis, Minnesota. Although Medtronic, Inc. does not regard these corporations as "affiliates," they are identified here in the interest of full and complete disclosure.

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BRIEF OF RESPONDENT IN OPPOSITION

OPINIONS BELOW

The Order dated January 10, 1985, of the United States District Court, Southern District of Florida, granting Petitioner's Motion for Establishment of Escrow Fund and for Preliminary Injunction is reported at 606 F. Supp. 132,

and is reproduced in Petitioner's Appendix at pages 10a-12a.

The panel decision of the United States Court of Appeals for the Federal Circuit dated December 17, 1985, vacating the District Court's Order is reported at 780 F.2d 991, and is reproduced in Petitioner's Appendix at pages 1a-8a. Petitioner's Petition for Rehearing and Suggestion for Rehearing In Banc was denied by Order dated February 14, 1986, a copy of which is reproduced in Petitioner's Appendix at page 9a.

JURISDICTION

See Petition at page 2 for jurisdictional ground asserted.

CONSTITUTIONAL PROVISIONS INVOLVED

See Petition at page 2.

STATEMENT OF THE CASE

1. Factual Background and the District Court's Decision.

Petitioner Cordis Corporation ("Cordis") and Respondent Medtronic, Inc. ("Medtronic") are parties to a License Agreement ("the License Agreement") pursuant to which Cordis is licensed to make, use, lease, and sell certain atrial and ventricular tined leads covered by two Medtronic patents (the "patents in suit"). Tined leads are surgically used in conjunction with implantable cardiac pacemaker pulse generators to conduct electrical signals between the pulse generator and the heart.

In late 1981 or early 1982, Cordis approached Medtronic seeking a license under the patents in suit. The License Agreement between the parties was entered into in late January or early February, 1982. (See App. A

at 43)[2] Prior to that time, Medtronic had been engaged in litigation with three of its domestic competitors, Intermedics, Inc., Pacesetter Systems, Inc., and Daig, Inc., over their infringement, and the challenged validity, of one of the two Medtronic patents that Cordis desired to license from Medtronic.[3] (See Rooney Aff., ¶¶ 3 and 4; App. A at 63-64) Cordis was aware of these controversies before it entered into the License Agreement. Recognizing that its alternatives

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2. References to "App. A" refer to the Appendix of Medtronic filed with the Court of Appeals for the Federal Circuit. References to "App." refer to the Appendix to Cordis' Petition for Writ of Certiorari.

3. Medtronic was also litigating its corresponding patents in
(Footnote Continued)

were to license the patents in suit or to risk patent litigation with Medtronic, Cordis chose the former alternative and the contractual benefits attendant to licensee status.

Cordis operated under the License Agreement for more than two years. In October 1984, Cordis' patent counsel threatened Medtronic "with a lawsuit . . . unless and until Medtronic would agree to escrowing royalty payments pending a decision" in Medtronic's patent litigation with its competitors, Pacesetter Systems, Inc. and Daig, Inc., then pending in the District of Minnesota. (See Rooney Aff. ¶ 10; App. A at 66)

When Medtronic refused Cordis' demand, Cordis commenced this action on October 19, 1984.

(Footnote Continued)
France and Germany. (See Rooney Aff. ¶ 5; App. A at 65)

By its Complaint, Cordis seeks a declaratory judgment that the patents in suit and the License Agreement itself are invalid. Cordis contemporaneously moved for an order establishing an escrow account for the deposit of royalty payments it owed Medtronic pursuant to the License Agreement, and for a preliminary injunction enjoining Medtronic from terminating the License Agreement during the pendency of the action.

The District Court (Hon. C. Clyde Atkins), by a three-page Order dated January 10, 1985, granted Cordis the relief it sought. (606 F. Supp. 132)

2. The Federal Circuit's Decision.

On December 17, 1985, the Court of Appeals for the Federal Circuit vacated the District Court's Order and remanded for further consideration. In so ruling, the Federal Circuit

determined that the District Court had misapplied Lear as mandating the creation of the escrow account sought by Cordis and the entry of the preliminary injunction enjoining Medtronic from terminating the License Agreement. Specifically, the Federal Circuit could:

> find no authority in Lear for establishing an escrow account for royalties due pendente lite or preliminarily enjoining a licensor from cancelling the license agreement and, thus, from counterclaiming for patent infringement when this material breach of the license occurs. (App. at 5a)

Focusing on language in Lear discussing the public interest underlying federal patent policy, the Federal Circuit concluded:

> This public policy statement does permit a licensee to cease payments due under a contract while challenging the validity of a patent. It does not permit the licensees to avoid facing the consequences that such an action would bring. The holding of Lear

> only prevents the affirmative enforcement by the licensor of the royalty payment provisions of the license agreement while the patent's validity is being challenged by the licensee. (App. at 6a) (emphasis in original)

The Federal Circuit went on to conclude that, in addition to misapplying Lear, the District Court made errors of law in applying the traditional standard for determining the propriety of granting a preliminary injunction. Specifically, it held that the District Court had erred in finding that Cordis had established the element of irreparable harm and in evaluating the likelihood of success factor.

REASONS FOR DENYING WRIT

I

Nothing in the Federal Circuit's Decision is Inconsistent with Lear, Inc. v. Adkins

Despite Cordis' attempt to wrap itself in the cloak of Lear, Inc. v. Adkins, 395 U.S. 653 (1969), the holding of Lear does not dispose of the issues here presented. Nor does the Lear dicta upon which Cordis relies, when considered in the context of the particular facts confronting this Court in Lear, support Cordis' position. The equities which buttressed the licensee's position in Lear are simply not present in this case. Moreover, the public interest considerations underlying federal patent law, which this Court determined compelled the result in Lear, compel a different result here.

A. Lear Does Not Compel the Relief Cordis Seeks

Neither the holding of Lear, nor its underlying rationale, compels the result Cordis seeks. As stated by Justice Harlan, and as underscored by Cordis at page 6 of its Petition, the "decisive question" in Lear was:

> whether overriding federal policies would be significantly frustrated if licensees could be required to continue to pay royalties during the time they are challenging validity in the courts. (Id. at 673) (emphasis supplied)

In contrast to Lear, Medtronic does not seek to require Cordis to do anything. Consistent with Lear, under the Federal Circuit's decision Cordis is free to determine for itself whether to continue to pay royalties to Medtronic, or to cease royalty payments during the pendency of this litigation brought by Cordis. Medtronic maintains only that, if

Cordis chooses not to honor its license obligations to Medtronic, it then has no right to the continued benefits under the License Agreement. In such event, Medtronic may terminate the License Agreement and counterclaim against Cordis for infringement of the patents in suit, as the Federal Circuit concluded.

While there is language in Lear which, in the abstract, might be generally viewed as preferring the rights of the licensee (Lear, Inc.) to those of the licensor (Adkins), that language must be considered in the context of the particular facts there before this Court.[4]

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4. Cf. Cohens v. Virginia, 19 U.S. (6 Wheat.) 264, 399 (1821) (Marshall, C.J.) ("It is a maxim not to be disregarded, that general expressions, in every

(Footnote Continued)

In Lear, the license agreement was entered into before any patent had issued. It called for the payment of royalties based upon the use of the claimed invention both before and during the life of any patent which might issue. Subsequent to negotiation of the license agreement, but prior to the issuance of the patent, Lear -- as licensee -- notified Adkins -- as licensor -- that Lear had found a patent which it believed fully anticipated Adkins' claimed invention. Lear then terminated all payments under the agreement and expressly repudiated the license agreement more than two years prior to the issuance of Adkins' patent. Thus, when Adkins brought suit, no

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(Footnote Continued)
opinion, are to be taken in connection with the case in which those expressions are used.")

contractual relationship existed between the parties. 395 U.S. at 659-660.

This Court initiated its analysis of the facts of Lear with an assessment of "the spirit of contract law, which seeks to balance the claims of promisor and promisee in accord with the requirements of good faith." Id. at 670. Only after satisfying itself that the equities were balanced did this Court proceed to consider the policy underlying the federal patent laws and the public interest.

In contrast to Lear, Cordis entered into the License Agreement knowing full well that the Medtronic patents it sought to license were the subject of ongoing litigation between Medtronic and third parties, and that their validity was at issue in that litigation. For more than two years, Cordis enjoyed the benefits and protection

of the License Agreement, the two licensed patents and the corresponding foreign patents. When it became expedient to do so, Cordis decided to join the other infringers of the patents in suit by belatedly challenging their validity in this declaratory judgment action.

Unlike Lear, however, Cordis did not repudiate its contractual relationship with its licensor, Medtronic. Rather, it brought suit and immediately sought to secure for itself the right to uninterrupted enjoyment of the fruits of the License Agreement, free of any obligation to make royalty payments to Medtronic, pending final resolution of this action. The inequity of Cordis' attempt to rewrite by judicial fiat its contract with Medtronic, to its sole benefit and Medtronic's detriment, stands in stark contrast to the position of the licensee in Lear.

B. The Public Interest Considerations Underlying Lear Support the Conclusion Reached by the Federal Circuit

The heart of Lear is this Court's effort to strike a middle ground between the sanctity of a bargained-for agreement, rooted in contract law, and the public interest in free access to ideas underlying federal patent law. See 395 U.S. at 668. In contrast to the emphasis in Lear on achieving a balance between these competing concerns, the approach advocated by Cordis, once a licensee challenges the validity of a licensed patent, would require the courts to disregard entirely the parties' bargain. Cordis prefers a result that guarantees to it, as licensee, all of its benefits under the License Agreement during the pendency of its patent validity challenge, while holding the licensor

(Medtronic) in contractual limbo, with none of its bargained-for benefits, and all of its bargained-for burdens, for the duration of this litigation.

In Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470, 480-81 (1974), this Court stated:

> The stated objective of the Constitution in granting the power to Congress to legislate in the area of intellectual property is to "promote the Progress of Science and useful Arts." The patent laws promote this progress by offering a right of exclusion for a limited period as an incentive to inventors to risk the often enormous costs in terms of time, research, and development. The productive effort thereby fostered will have a positive effect on society through the introduction of new products and processes of manufacture into the economy, and the emanations by way of increased employment and better lives for our citizens.

* * *

> When a patent is granted and the information contained in it is circulated to the general public and those especially skilled in the trade, such additions to the general store of knowledge are of such importance to the public weal that the Federal Government is willing to pay the high price of 17 years of exclusive use for its disclosure, which disclosure, it is assumed, will stimulate ideas and the eventual development of further significant advances on the art.

The exclusive rights conferred by a patent grant, then, are designed not only to encourage invention, but more importantly to encourage the disclosure of the invention to the public.

To foster the public interest in disclosure of inventions by encouraging resort to the patent system in the first instance, as well as the subsequent licensing of issued patents, it is imperative that there be a perceptibly fair balance between the rights of the

licensor and those of the licensee. To prefer, by such a great measure, the interests of the licensee to those of the licensor, as the District Court did and as Cordis urges, seriously risks undermining the incentives an inventor will have to share his invention through conventional licensing arrangements. As one commentator noted in this regard:

> Any rule of law that discourages licensing, one of the main benefits of owning a patent, conflicts with the policy that encourages inventors to use the patent system, and any interpretation of Lear that pushes inventors away from the patent system cannot be within the true spirit of either Lear or federal patent policy.

J. McCarthy, "Unmuzzling" The Patent Licensee: Chaos in the Wake of Lear v. Adkins (Part I), 59 J. Patent Office Society 475, 496 (1977).

The "licensee choice" rule reflected in the Federal Circuit's

decision, here challenged by Cordis, is a fair solution to the question of how traditional contract law should be shaped to give licensees adequate incentive to challenge patent validity consistent with Lear's emphasis on balancing the equities among licensor, licensee, and the public interest.[5] As the Federal Circuit

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5. Legislation sponsored by the Administration and now pending in Congress recognizes the need for the same kind of balance. Title VII of the Intellectual Property Rights Improvement Act of 1986 would add a new Section 296 to Title 35, United States Code, to address the rights of licensees to challenge the validity of patents they have licensed and the corresponding rights of patent holders in such circumstances. Proposed new Section 296(a) codifies the holding of Lear by providing that a licensee shall not be estopped from asserting the invalidity of a patent to which it licensed. Proposed new Section

(Footnote Continued)

recognized, Lear permits a licensee to challenge patent

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296(b) addresses the rights of the parties with respect to termination of the license and payment of royalties if the licensee challenges the validity of the licensed patent.

As described in the Section-by-Section Analysis of the proposed Act released by the Office of the U.S. Trade Representative on April 7, 1986:

> New Section 296(b) would give the parties broad discretion to define these rights during the license negotiation process. It makes clear that the parties may provide for termination by licensor and/or licensee in the event of such a challenge, and, if the licensee has a right to terminate, for the licensee's obligations to continue pending adjudication of validity. In this way, patent licensors can bargain for provisions they feel necessary to assure the realization of their rights
>
> (Footnote Continued)

validity and not pay royalties during the challenge period. If

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(Footnote Continued)

> in an invention, while licensees can bargain for provisions they feel necessary to protect their interests if they choose to challenge validity. (emphasis supplied)

See Administration's Statement on Protection of U.S. Intellectual Property Rights Abroad, Draft Bill Entitled "Intellectual Property Rights Improvement Act of 1986" and Section-by-Section Analysis of Draft Bill, Released by Office of the U.S. Trade Representative, April 7, 1986, 31 Patent, Trademark & Copyright Journal (BNA) 506, 516 (April 10, 1986).

The License Agreement negotiated by Cordis with Medtronic provides for termination in the event "either party shall materially breach any of the terms, conditions and agreements contained in this Agreement," (License Agreement, § 10.02(a), App. A at 37), which would obviously include the failure by Cordis to pay royalties as due

(Footnote Continued)

the licensee elects this option, however, it should not be permitted to hide behind the protection of a license agreement as a shield against a claim of patent infringement. Nor, under the Federal Circuit's decision, is a licensor, in this situation, precluded from terminating the license agreement because of the licensee's breach for non-payment of royalties. If the licensee wishes to "hedge its bet" on patent invalidity by protecting itself against a claim of infringement, it can do so by continuing to pay the royalties due its licensor under its license agreement.

The balance struck between the rights of licensees and licensors by the Federal Circuit

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(Footnote Continued)
during a patent validity challenge.

accommodates the public interest in "unmuzzling" licensees to challenge invalid patents, see Lear, 395 U.S. at 670, without eliminating the equally important public interest in providing incentives for inventor/licensors to obtain and license patents. In its balancing of both public interest considerations, the Federal Circuit's decision is wholly consistent with Lear, thus raising no issue worthy of this Court's discretionary review.

Cordis' protestations notwithstanding, the decision of the Federal Circuit in this case does not present Cordis with:

> a "Hobson's choice"[6] which frustrates the overriding

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6. Although Cordis insists that it is confronted with a "Hobson's choice," that is clearly not the case. A "Hobson's choice," according to Webster's Third New

(Footnote Continued)

> federal policies of Lear just as surely as actually ordering that royalties be paid during the litigation. (Petition at 7); (footnote added)

The consequence to Cordis of the Federal Circuit's decision is that it must continue to honor the terms of the License Agreement if it wishes to enjoy the benefits of that contract during the pendency of this action. Cordis may thereby continue to enjoy the use

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(Footnote Continued) International Dictionary, properly refers to an apparent freedom of choice where none exists. The term derives from the practice of an English liveryman, named Hobson, who required every customer to rent the horse which was stabled nearest to the stable door. Cordis concedes that the Federal Circuit's decision leaves it with several options, albeit ones which Cordis finds unpalatable. By definition, Cordis is not confronted with a Hobson's choice.

of the patents in suit, which are presumed to be valid and which twice have been adjudicated to be valid, while it pursues its validity challenge.[7] In addition,

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7. In Medtronic, Inc. v. Intermedics, Inc., Civil No. G-80-295 (S.D. Tex., Galveston Division), the jury, in August 1983, returned a verdict finding Medtronic's Citron/Dickhudt patent, one of the two patents in suit, to be valid and infringed. In response to the motion of Intermedics for a new trial based on the discovery of alleged "new evidence," the District Court (Hon. Hugh Gibson) deferred entry of judgment on the jury verdict pending a decision by the United States District Court for the District of Minnesota in Medtronic, Inc. v. Daig Corporation, Civil No. 4-79-256 (D. Minn.), a case involving the same Medtronic patent in which the alleged "new evidence" had been presented. In June 1985, the Minnesota District Court (Hon. Earl R. Larson) ruled that the Medtronic patent was valid and

(Footnote Continued)

under the terms of the License Agreement, Medtronic is obligated to license or prosecute infringers of the patents in suit whose net sales exceeded specified limits, thereby providing Cordis with protection against competition from unlicensed competitors. (See License Agreement § 9.01; App. A at 35-36) In Lear, this Court observed that "[e]ven in the case of nonexclusive licenses, . . . competition is limited to the extent that the royalty charged by

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(Footnote Continued)
infringed. Thereafter, by Order dated October 4, 1985, the Texas District Court denied Intermedics' post trial motions and entered judgment for Medtronic. The decisions in both the Minnesota and Texas actions are currently on appeal to the Federal Circuit. See Daig Corporation v. Medtronic, Inc., Appeal No. 85-2645, and Medtronic, Inc. v. Intermedics, Inc., Appeal No. 86-647 (United States Court of Appeals for the Federal Circuit).

the patentee serves as a barrier to entry." 395 U.S. at 669, n.16. Finally, in addition to the use of the patents in suit, Cordis continues to enjoy the right to use the corresponding foreign patents. (See License Agreement § 1.05; App. A at 3)

In contrast to the option afforded Cordis to continue receiving the benefits of the License Agreement, while at the same time contesting the validity of the licensed patents, the District Court's Order in this case, and the position urged by Cordis, would deprive Medtronic of any similar option to enjoy the benefit of its bargain during the pendency of this litigation. By permitting Cordis to escrow royalties, Medtronic would be effectively deprived of any benefit of the License Agreement

throughout this litigation.[8] That Medtronic ultimately might be entitled to the escrowed royalties does not alleviate the harm to Medtronic from being deprived of receiving Cordis' royalty payments during the time the License Agreement remains in effect, while Medtronic remains obligated to defend the patents in suit against other infringers at Medtronic's expense, and also while Medtronic is confronted with the expenses of defending against Cordis' patent invalidity claims.

In sum, in its lopsided preference for the rights of the licensee to those of the licensor,

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8. As one court has correctly noted, in the eyes of the law, payment of royalties to an escrow agent is tantamount to non-payment. PPG Industries, Inc. v. Westwood Chemical, Inc., 530 F.2d 700, 705 (6th Cir.), cert. denied, 429 U.S. 824 (1976).

the position urged by Cordis as an extension of Lear is clearly contrary to the delicate balancing of competing public interests which lies at the heart of Lear, and, accordingly, is not deserving of discretionary review by this Court.

II

The Federal Circuit's Decision is Based Upon the Application of Well-Settled Principles Governing the Issuance of Injunctive Relief to Specific Facts and Thus Does not Present "an Important Question of Federal Law Which has not Been, but Should be, Settled by This Court" (Sup. Ct. R. 17.1(c))

The Federal Circuit's decision applied traditional and well-settled principles for appellate review of a grant of injunctive relief to the facts presented to it. Applying the traditional four-pronged test for granting a preliminary injunction, the Federal Circuit concluded that the District Court committed errors of law in holding that Cordis had demonstrated the likelihood of irreparable harm necessary for issuance of a preliminary injunction and in evaluating the likelihood of success factor. (App. at 6a-8a)

Nothing in the Federal Circuit's review of the District Court's application of the preliminary injunction standard constitutes the deciding of "an important question of federal law which has not been, but should be, settled by this Court" within the meaning of Supreme Court Rule 17.1(c), so as to warrant the exercise by this Court of discretionary review.

Cordis attempts to create an issue of unsettled federal law by inviting this Court to decide whether royalties paid by a licensee during a patent validity challenge are ultimately recoverable by the licensee, if the patent is ultimately held invalid. See Petition at 10-13. The Federal Circuit properly declined to decide that issue in the context of the appeal before it. (App. at 8a) Cordis, nonetheless, persists in arguing that the question of whether a licensee may

escrow royalties during the pendency of its patent validity challenge, and the question of ultimate entitlement to royalties paid during a patent validity challenge, are inextricably entertwined. Thus, at page 9 of its Petition, Cordis argues that:

> Such an escrow arrangement clearly eliminates the "chilling effect" imposed on the challenger-licensee because of the uncertainty about repayment of royalties.

Although neither this Court, nor the Federal Circuit, has addressed the "ultimate entitlement" issue, the resolution of that issue cannot rationally depend on whether royalties had been paid to a patentee-licensor during the pendency of the litigation or into an escrow fund. The situs of royalty payments pendente lite is not determinative of the question of ultimate entitlement. See, e.g., USM Corp. v. Standard

Pressed Steel, 524 F.2d 1097, 1099 (7th Cir. 1975), and cases cited therein. Thus, the Federal Circuit's resolution of the escrow fund issue did not decide the "ultimate entitlement" issue. That issue simply is not properly before this Court.

III

There is no Conflict in the Circuits Sufficient to Warrant the Exercise by This Court of its Discretionary Review

Cordis contends (Petition, 10-13) that there is a conflict among the circuits sufficient to warrant this Court's exercise of its discretionary review. No such conflict exists. By creating the United States Court of Appeals for the Federal Circuit, and vesting in it exclusive appellate jurisdiction in patent cases (28 U.S.C. § 1295), Congress eliminated any possibility of conflicting views among the federal appellate courts on patent matters. Prior decisional law of the other federal circuit courts is superseded by the Federal Circuit's decision below. To the extent the District Court perceived a conflict among the other federal circuits at the time it rendered its initial

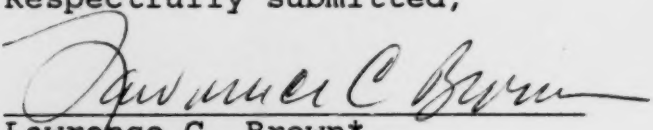
order, that "conflict" has been resolved now that the Federal Circuit has spoken.

CONCLUSION

This Court should deny the requested relief.

Dated: April 29, 1986

Respectfully submitted,



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